

**Deaconess Women's Hospital of Southern Indiana, LLC
d/b/a The Women's Hospital**

Accountants' Report and Financial Statements
December 31, 2011 and 2010

Deaconess Women's Hospital of Southern Indiana, LLC
d/b/a The Women's Hospital
December 31, 2011 and 2010

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Independent Accountants' Report

Board of Managers
Deaconess Women's Hospital of
Southern Indiana, LLC
d/b/a The Women's Hospital
Newburgh, Indiana

We have audited the accompanying balance sheets of Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital (Hospital) as of December 31, 2011 and 2010, and the related statements of income, members' equity and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

BKD, LLP

February 6, 2012

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Balance Sheets December 31, 2011 and 2010

Assets

	2011	2010
Current Assets		
Cash and cash equivalents	\$ -	\$ 3,502,555
Accounts receivable, net of allowance for uncollectible accounts; 2011 - \$924,793, 2010 - \$931,858	8,291,220	7,522,084
Supplies	383,429	373,956
Prepaid expenses and other	592,996	319,403
Total current assets	<u>9,267,645</u>	<u>11,717,998</u>
Property and Equipment, at cost		
Leasehold improvements	1,222,167	1,204,617
Equipment	12,036,037	11,924,195
Construction in progress	205,323	95,920
	<u>13,463,527</u>	<u>13,224,732</u>
Less accumulated depreciation	<u>(9,204,329)</u>	<u>(8,265,185)</u>
	<u>4,259,198</u>	<u>4,959,547</u>
Other Assets		
Other assets	191,213	177,705
Goodwill	295,800	295,800
	<u>487,013</u>	<u>473,505</u>
Total assets	<u>\$ 14,013,856</u>	<u>\$ 17,151,050</u>

Liabilities and Members' Equity

Current Liabilities		
Checks in process of clearing	\$ 686,336	\$ -
Line of credit	1,521,870	-
Current maturities of long-term debt	439,911	581,510
Accounts payable	2,846,740	2,528,330
Accrued expenses	1,874,532	1,725,872
Total current liabilities	<u>7,369,389</u>	<u>4,835,712</u>
Long-Term Debt	<u>512,948</u>	<u>899,827</u>
Members' Equity		
Contributed capital	3,500,000	3,500,000
Accumulated earnings	2,631,519	7,915,511
Total members' equity	<u>6,131,519</u>	<u>11,415,511</u>
Total liabilities and members' equity	<u>\$ 14,013,856</u>	<u>\$ 17,151,050</u>

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Statements of Income Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Revenues		
Net patient service revenue	\$ 49,598,541	\$ 53,929,171
Other	<u>1,687,597</u>	<u>1,445,151</u>
Total revenue, gains and other support	<u>51,286,138</u>	<u>55,374,322</u>
Expenses and Losses		
Salaries and wages	18,787,617	17,988,224
Employee benefits	5,352,363	4,994,325
Medical supplies	3,647,233	3,811,727
General supplies	1,158,156	1,056,260
Purchased services and professional fees	10,148,273	9,778,433
Rent expense	3,620,278	3,593,064
Depreciation and amortization	1,154,675	1,252,126
Interest expense	123,352	152,758
Provision for uncollectible accounts	1,246,561	1,285,190
Loss on disposal of equipment	(5,295)	24,480
Other	<u>3,088,798</u>	<u>3,051,143</u>
Total expenses and losses	<u>48,322,011</u>	<u>46,987,730</u>
Operating Income	2,964,127	8,386,592
Other Income		
Interest income	<u>5,765</u>	<u>7,170</u>
Net Income	<u><u>\$ 2,969,892</u></u>	<u><u>\$ 8,393,762</u></u>

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Statements of Members' Equity Years Ended December 31, 2011 and 2010

	Contributed Capital	Accumulated Earnings	Total
Balance, January 1, 2010	\$ 3,500,000	\$ 2,501,358	\$ 6,001,358
Net income	-	8,393,762	8,393,762
Distributions to members	-	(2,979,609)	(2,979,609)
Balance, December 31, 2010	3,500,000	7,915,511	11,415,511
Net income	-	2,969,892	2,969,892
Distributions to members	-	(8,253,884)	(8,253,884)
Balance, December 31, 2011	<u>\$ 3,500,000</u>	<u>\$ 2,631,519</u>	<u>\$ 6,131,519</u>

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Statements of Cash Flows Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Operating Activities		
Net income	\$ 2,969,892	\$ 8,393,762
Items not requiring (providing) cash		
Depreciation and amortization	1,154,675	1,252,126
Provision for uncollectible accounts	1,246,561	1,285,190
(Gain) loss on sale of property and equipment	(5,295)	24,480
Changes in		
Patient accounts receivable	(2,015,697)	(1,510,024)
Supplies	(9,473)	(42,490)
Accounts payable and accrued expenses	467,070	(58,878)
Other assets	(287,101)	(85,297)
Net cash provided by operating activities	<u>3,520,632</u>	<u>9,258,869</u>
Investing Activities		
Proceeds from sale of property and equipment	9,705	-
Purchase of property and equipment	(424,256)	(1,059,184)
Net cash used in investing activities	<u>(414,551)</u>	<u>(1,059,184)</u>
Financing Activities		
Increase (decrease) in checks in process of clearing	686,336	(609,392)
Net borrowings (payments) under line of credit agreement	1,521,870	(720,210)
Distributions to members	(8,253,884)	(2,979,609)
Proceeds from issuance of long-term debt	-	200,239
Principal payments on long-term debt and capital leases	(562,958)	(588,158)
Net cash used in financing activities	<u>(6,608,636)</u>	<u>(4,697,130)</u>
Change in Cash	(3,502,555)	3,502,555
Cash, Beginning of Year	<u>3,502,555</u>	<u>-</u>
Cash, End of Year	<u>\$ -</u>	<u>\$ 3,502,555</u>
Supplemental Cash Flows Information		
Interest paid	\$ 127,554	\$ 151,916
Capital lease obligation incurred for property and equipment	34,480	515,988

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Notes to Financial Statements December 31, 2011 and 2010

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital (Hospital) primarily earns revenues by providing obstetrical, gynecological and nursery care on an inpatient and outpatient basis to women in Evansville, Indiana and surrounding communities. The Hospital is organized as a limited liability company; therefore, taxable income or loss is reported to the individual members of the corporation for inclusion in their respective tax returns.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Risk Management

The Hospital is exposed to various risks of loss from torts, theft of, damage to and destruction of assets, business interruption, errors and omissions, employee injuries and illnesses, natural disasters and employee health benefits. Commercial insurance coverage is purchased for claims arising from such matters.

Supplies

The Hospital states supply inventories at the lower of cost, determined using the first-in, first-out (FIFO) method or market.

Property and Equipment

Property and equipment are stated at cost and depreciated over the estimated useful life of each asset. Leasehold improvements are amortized over the shorter of the lease term or the estimated useful lives of the improvements. Annual depreciation is primarily computed using straight-line methods.

Charity Care

The Hospital provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Charity care is not reported as revenue. Charges excluded from revenue under the Hospital's charity care policy were \$231,152 and \$204,301 for 2011 and 2010, respectively. Total cost for these charges based on the Hospital's overall cost-to-charge ratio was approximately \$105,752 and \$93,467 for 2011 and 2010, respectively.

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Notes to Financial Statements December 31, 2011 and 2010

Cash and Cash Equivalents

Effective July 21, 2010, the FDIC insurance limits were permanently increased to \$250,000. At December 31, 2011, the Hospital's deposit accounts were fully insured.

Checks in Process of Clearing

The Hospital has an arrangement with a bank whereby any cash held at the end of each banking day is swept against the outstanding balance of the line of credit (see Note 4). The arrangement also directs the bank to transfer cash from the line of credit to the cash accounts to pay checks as they are processed through the bank. The result is a credit amount in the cash account, which represents checks written by the Hospital but not yet processed by the bank.

Patient Accounts Receivable

Patient accounts receivable are stated at net realizable amounts from patients, third-party payers and others for services rendered. The Hospital provides an allowance for doubtful accounts, which is based upon a review of outstanding receivables, historical collection information and existing economic conditions. Patient accounts receivable are ordinarily due 30 days after the issuance of the patient statement. Balances past due more than 120 days are considered delinquent. Delinquent receivables are written off based on individual credit evaluation and specific circumstances of the patient or third-party payer.

Goodwill

Goodwill is tested annually for impairment. If the implied fair value of goodwill is lower than its carrying amount, a goodwill impairment is indicated and goodwill is written down to its implied fair value. Subsequent increases in goodwill value are not recognized in the financial statements.

Long-Lived Asset Impairment

The Hospital evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value. No asset impairment was recognized during the years ended December 31, 2011 and 2010.

Limited Liability Company

The Hospital is organized as an Indiana limited liability company and is governed by an eight-member board of managers. The board of managers is generally responsible for the direction and management of the Hospital. The Hospital is owned by two members, each with 50% ownership.

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Notes to Financial Statements December 31, 2011 and 2010

Income Taxes

The Hospital's members have elected to have the Hospital's income taxed as a partnership under provisions of the Internal Revenue Code and a similar section of the state income tax law. Therefore, taxable income or loss is reported to the individual members for inclusion in their respective tax returns and no provision for federal and state income taxes is included in these financial statements. The Hospital's tax years still subject to examination by taxing authorities are years subsequent to December 31, 2007.

Subsequent Events

Subsequent events have been evaluated through the date of the Independent Accountants' Report, which is the date the financial statements were available to be issued.

Note 2: Net Patient Service Revenue

The Hospital has agreements with third-party payers that provide for payments to the Hospital at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. These payment arrangements include:

Managed care. The Hospital has entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

Medicaid. Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. Outpatient reimbursement is based on prospectively established fee schedule allowances and rates for surgery groups.

The Hospital qualifies as a Medicaid Disproportionate Share Hospital (DSH) provider under Indiana law and, as such, is eligible to receive supplemental Medicaid payments. The amounts of these supplemental payments are dependent on regulatory approval by agencies of the federal and state governments and is determined by level, extent and cost of uncompensated care (as defined) and various other factors. Supplemental payments have been made by the State of Indiana, and the Hospital records such amounts as revenue when it has been reasonably determined that the funds will be received. The Hospital recognized \$2,443,285 and \$6,505,618 of net patient service revenue related to the supplemental payment program for the years ended December 31, 2011 and 2010, respectively.

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Notes to Financial Statements December 31, 2011 and 2010

Effective January 1, 2008, the State of Indiana began operating an insurance plan for the benefit of Indiana residents without health insurance. The plan, referred to as the Healthy Indiana Plan (HIP), is funded through an additional state cigarette tax and with the use of a portion of the DSH funds described above. As such, the level of future Medicaid supplemental payments may also be negatively affected.

Approximately 95% of net patient service revenues are from participation in managed care and state-sponsored Medicaid program for the years ended December 31, 2011 and 2010. Laws and regulations governing the Medicaid program are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

Note 3: Concentration of Credit Risk

The Hospital grants credit without collateral to its patients, most of whom are area residents and are insured under third-party payer agreements. The mix of receivables from patients and third-party payers at December 31 was:

	2011	2010
Medicare	1%	2%
Medicaid	13	20
Other third-party payers	73	64
Patients	13	14
	100%	100%

Note 4: Line of Credit

The Hospital has a \$4,000,000 revolving line of credit expiring in May 2012. At December 31, 2011 and 2010, there was \$1,521,870 and \$0, respectively, borrowed under this line of credit. The line of credit is collateralized by substantially all of the Hospital's assets. Interest varies with the London Interbank Offered Rate (LIBOR) plus 1.9% and is payable monthly. The interest rate was 3.00% on December 31, 2011.

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Notes to Financial Statements December 31, 2011 and 2010

Note 5: Long-Term Debt

	2011	2010
Note payable, bank (A)	\$ 83,969	\$ 227,338
Capital lease obligations (B)	760,225	1,080,123
Note payable (C)	108,665	173,876
	<u>952,859</u>	<u>1,481,337</u>
Less current maturities	<u>439,911</u>	<u>581,510</u>
	<u>\$ 512,948</u>	<u>\$ 899,827</u>

- (A) Due October 2012; payable \$14,758 monthly including interest at 6.64%; secured by substantially all assets of the Hospital. The Hospital is required to comply with certain financial covenants.
- (B) Capital leases include leases for various equipment for terms ranging from 4 to 20 years. The leases assume interest rates of 2.98% to 8.25%. The leases are payable in monthly installments ranging from \$968 to \$6,332 and are secured by the leased equipment.
- (C) Due July 2013; payable \$5,907 monthly including interest at 3.88%; secured by equipment.

Aggregate annual maturities of long-term debt and payments on capital lease obligations at December 31, 2011 were:

	Long-Term Debt (Exc. Leases)	Capital Lease Obligations
2012	\$ 151,781	\$ 322,131
2013	40,853	253,798
2014	-	158,617
2015	-	92,863
2016	<u>-</u>	<u>7,327</u>
	<u>\$ 192,634</u>	834,736
Less amount representing interest		<u>74,511</u>
Present value of future minimum lease payments		<u>\$ 760,225</u>

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Notes to Financial Statements December 31, 2011 and 2010

Property and equipment include the following property under capital leases:

	2011	2010
Equipment	\$ 2,209,327	\$ 2,236,247
Less accumulated depreciation	<u>1,556,766</u>	<u>1,303,404</u>
	<u><u>\$ 652,561</u></u>	<u><u>\$ 932,843</u></u>

Note 6: Operating Leases

Noncancellable operating leases for the building and equipment expire at various dates through 2030. The leases require the Hospital to pay all executory costs (property taxes, maintenance and insurance).

Future minimum lease payments at December 31, 2011 were:

2012	\$ 3,646,639
2013	3,620,551
2014	3,510,244
2015	3,419,781
2016	3,392,456
Later years	<u>49,857,876</u>
	<u><u>\$ 67,447,547</u></u>

Rent expense for all operating leases was \$3,620,278 and \$3,593,064 for the years ended December 31, 2011 and 2010, respectively.

Note 7: Profit-Sharing Plan

The Hospital has a 401(k) profit-sharing plan (Plan) covering substantially all employees. The Hospital's contributions to the Plan are determined annually by the board of managers. Contributions to the Plan were \$379,453 and \$350,693 for 2011 and 2010, respectively.

Note 8: Deferred Compensation Agreement

The Hospital has a deferred compensation agreement with the chief executive officer that provides certain benefits upon disability or retirement. The present value of total estimated deferred compensation is being accrued using the straight-line method over the remaining years to the full eligibility date. Expense for 2011 and 2010 was \$18,380.

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Notes to Financial Statements December 31, 2011 and 2010

Note 9: Related Party Transactions

Deaconess Hospital, Inc. (DHI) owns 50% of the Hospital. The Hospital engages in various transactions with DHI, which are summarized below.

- Capital lease arrangements - The Hospital leases various equipment under capital lease arrangements from DHI. Payments related to these leases totaled \$122,114 and \$149,189 for 2011 and 2010. Amounts owed at December 31, 2011 and 2010 totaled \$227,383 and \$326,442, respectively, and the net book value of the related equipment was \$154,357 and \$230,003 for 2011 and 2010, respectively. These leases are also included and described in Note 5.
- Operating lease arrangements - The Hospital leases its hospital, education and office space from DHI under noncancellable leases ranging from 10 to 30 years. Total payments under these arrangements were \$3,143,838 and \$3,091,645 in 2011 and 2010, respectively. These leases are also included and described in Note 6.
- Other services - The Hospital contracts with DHI for pharmacy, lab, transcription, coding and other services. Payments made to DHI under these agreements totaled \$2,581,881 and \$2,424,670 in 2011 and 2010, respectively. Amounts included in accounts payable for these services at year end totaled \$934,041 and \$981,459 in 2011 and 2010, respectively.

Note 10: Malpractice Claims

The Hospital purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. Additionally, the Hospital is a qualified health care provider under the Indiana Medical Malpractice Act and is fully insured under a claims-made policy on a fixed premium basis. The Indiana Medical Malpractice Act limits a qualified provider's liability for an occurrence to the amount of required insurance. The Indiana patient compensation fund is liable for the excess up to an overall damage cap. Accounting principles generally accepted in the United States of America requires a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. The total amount accrued at December 31, 2011 is \$198,000, which is also recorded as a receivable at December 31, 2011, as management believes the amounts accrued at year end are also fully covered by purchased insurance. It is reasonably possible that this estimate could change materially in the near term.

Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital

Notes to Financial Statements December 31, 2011 and 2010

Note 11: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America requires disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

Current Economic Conditions

The current protracted economic decline continues to present hospitals with difficult circumstances and challenges, which in some cases have resulted in large and unanticipated declines in the fair value of assets, constraints on liquidity and capital and difficulty obtaining financing. The financial statements have been prepared using values and information currently available to the Hospital.

Current economic conditions, including the rising unemployment rate, have made it difficult for certain of our patients to pay for services rendered. As employers make adjustments to health insurance plans or more patients become unemployed, services provided to self-pay and other payers may significantly impact net patient service revenue, which could have an adverse impact on the Hospital's future operating results. Further, the effect of economic conditions on the state may have an adverse effect on cash flows related to the Medicaid program.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in asset values and allowances for accounts receivable that could negatively impact the Hospital's ability to meet debt covenants or maintain sufficient liquidity.

Allowance for Net Patient Service Revenue Adjustments

Estimates of allowances for adjustments included in net patient service revenue are described in Notes 1 and 2.

Admitting Physicians

The Hospital is served by one group of admitting physicians whose patients comprise approximately 30% and 33% of the Hospital's net patient service revenue for 2011 and 2010, respectively.

Deferred Compensation Agreement

As described in Note 8, the amount of annual expense accrued for deferred compensation is based on an estimate of the total amounts payable under the contract over the lifetime of the beneficiary.